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7 UNITED STATES DISTRICT COURT
8 WESTERN DISTRICT OF WASHINGTON
AT TACOMA

9 ALPHA VENTURE CAPITAL PARTNERS
10 LP, CARACCIOLO FAMILY TRUST,
11 GREGORY A. GOULD, LAW OFFICES
12 OF KENNETH E. CHYTEN 401(k) PROFIT
SHARING PLAN, GAVIN
MYERS, AND MARTIN PETERSON,
derivatively on behalf of CYTODYN, INC.,

13
14 Plaintiffs,

15 v.

16 NADER Z. POURHASSAN,

17 Defendant,

18 -and-

19 CYTODYN, INC., a Delaware Corporation,

20 Nominal Defendant.
21
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25
26

No.

COMPLAINT FOR VIOLATION OF THE
SECURITIES EXCHANGE ACT OF 1934

COMPLAINT FOR VIOLATION OF THE SECURITIES
EXCHANGE ACT OF 1934 - 1
Case No.

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**COMPLAINT FOR VIOLATION
OF THE SECURITIES EXCHANGE ACT OF 1934**

On behalf of Nominal Defendant CytoDyn, Inc., (“CytoDyn” or the “Company”), plaintiffs Alpha Venture Capital Partners LP, Caracciolo Family Trust, Gregory Gould, Law Offices of Kenneth E. Chyten 401(k) Profit Sharing Plan, Gavin Myers, and Martin Peterson (“Plaintiffs”) assert a claim against Defendant Nader Z. Pourhassan (“Pourhassan”), Chief Executive Officer of CytoDyn, Inc. (“CytoDyn” or the “Company”), for violation of the Securities Exchange Act of 1934.

NATURE AND SUMMARY OF THE ACTION

1. This is a strict liability action to recover illicit short-swing profits under Section 16(b) of the United States Securities Exchange Act of 1934 (the “Exchange Act”), 15 U.S.C. § 78p(b).

2. On December 19, 2019, Nader Pourhassan (“Pourhassan”), the Company’s Chief Executive Officer (“CEO”), was granted stock options to purchase 2,000,000 shares of CytoDyn common stock at an exercise price of \$0.63 per share (the “December 2019 Grant”).¹

3. Between April 30 and May 4, 2020, less than six months after he was awarded the December 2019 Grant, Pourhassan sold 4,821,174 shares of CytoDyn common stock – at prices ranging from \$2.53 to \$3.74 per share – which included the exercise of the December 2019 Grant and the sale of such shares.

4. Pourhassan’s deemed purchase and sale of CytoDyn securities within six months is a violation of Section 16(b) of the Exchange Act (“Section 16(b)”), and the transactions are not subject to any liability exemption, including but not limited to SEC Rule 16b-3 (“Rule 16b-3”). Accordingly, Pourhassan is subject to strict liability under Section 16(b) and must disgorge his profits from this illegal transaction.

¹ At the same time, Pourhassan was also awarded 2,000,000 shares subject to a stock purchase warrant, with the same \$0.63 per share exercise price.

PARTIES

5. Plaintiffs are six current holders of CytoDyn common stock that collectively beneficially own more than 11.8 million shares.

6. Plaintiff Alpha Venture Capital Partners, L.P. (“Alpha”) is a stockholder of CytoDyn and continuously held CytoDyn common stock since October 2013. Alpha beneficially owns approximately 1,000 shares of CytoDyn common stock. Carl Dockery, Alpha’s founder and the manager of Alpha’s general partner, is a former director of CytoDyn who served on the CytoDyn’s Board of Directors (the “Board”) from September 2014 until September 2019.

7. Plaintiff Caracciolo Family Trust (“CFT”) is a stockholder of CytoDyn and continuously held CytoDyn common stock since 2011. CFT beneficially owns approximately 1.7 million shares of CytoDyn common stock. Anthony Caracciolo (“Caracciolo”), the sole trustee of CFT, is a former executive and director of CytoDyn who served on the Board from January 2011 until December 2018. Caracciolo served as Chairman of the Board from June 2013 until December 2018. From January 2017 until July 2018, Caracciolo also served as Executive Chairman.

8. Plaintiff Gregory A. Gould (“Gould”) is a stockholder of CytoDyn and continuously held CytoDyn common stock since 2002. Gould beneficially owns approximately 10,000 shares of CytoDyn common stock. Gould is a former director of CytoDyn who served on the Board from 2006 until August 2019. Gould also served as Chairman of the Board, preceding Caracciolo, until July 2013.

9. Plaintiff Law Offices of Kenneth E. Chyten 401(k) Profit Sharing Plan (“KEC 401(K) Plan”) is a stockholder of CytoDyn and continuously held CytoDyn common stock since 2015. KEC 401(k) Plan beneficially owns approximately 284,000 shares of CytoDyn common stock.

1 10. Plaintiff Gavin Myers is a stockholder of CytoDyn and continuously held
2 CytoDyn common stock since 2013. Mr. Myers beneficially owns approximately 7,000 shares of
3 CytoDyn common stock.

4 11. Plaintiff Martin Peterson is a stockholder of CytoDyn and continuously held
5 CytoDyn common stock since 2017. Mr. Peterson beneficially owns approximately 5,000 shares
6 of CytoDyn common stock.

7 12. Nominal Defendant CytoDyn is a Delaware corporation and its principal
8 executive offices are located at 1111 Main Street, Suite 660, Vancouver, Washington 98660.
9 CytoDyn is publicly-traded on the OTC market under the ticker symbol "CYDY."

10 13. Defendant Pourhassan served as the Company's CEO, President, and Board
11 member since 2012. He was appointed to the CytoDyn Board in September 2012, and became
12 the Company's President and CEO in December 2012, following his service as interim President
13 and CEO for the preceding three months.

14 **JURISDICTION AND VENUE**

15 14. Jurisdiction of this Court and venue in this District are proper according to
16 15 U.S.C. § 78aa because Defendant Pourhassan maintains an office and/or transacts business in
17 this District, Nominal Defendant CytoDyn maintains its principal place of business in this
18 District, and certain acts of the underlying action occurred in this District.

19 **SUBSTANTIVE ALLEGATIONS**

20 **I. Pourhassan receives 2 million stock options in December 2019.**

21 15. In December 2019, the Board comprised Pourhassan and four purportedly non-
22 employee directors: Scott A. Kelly ("Kelly"), Michael A. Klump ("Klump"), Jordan G.
23 Naydenov ("Naydenov"), and David F. Welch ("Welch") (the "December 2019 Board").

24 16. On December 19, 2019, Pourhassan received a grant of stock options to purchase
25 2,000,000 shares of CytoDyn common stock at an exercise price of \$0.63 per share, i.e., the
26 December 2019 Grant.

1 17. On December 23, 2019, the Company disclosed the December 2019 Grant in a
2 Form 4 filing with the SEC.

3 **II. Less than six months later, Pourhassan sells 4.8 million shares of CytoDyn common**
4 **stock, including the 2 million option shares he received in the December 2019 Grant.**

5 18. Between April 30 and May 4, 2020, Pourhassan sold 4,821,174 shares of
6 CytoDyn common stock, at prices ranging from \$2.53 per share to \$3.74 per share (the “Sales”).

7 19. CytoDyn disclosed the Sales in a Form 4 filed with the SEC on May 4, 2020.
8 Specifically, the Form 4 disclosed the following sales of CytoDyn common stock: (1) On April
9 30, 2020, Pourhassan sold 2,219,837 shares of CytoDyn common stock at prices ranging from
10 \$3.44 to 3.74 per share, at a weighted average sale price of \$3.5312 per share; (2) On May 1,
11 2020, Pourhassan sold 1,399,685 shares of CytoDyn common stock at prices ranging from \$3.13
12 to \$3.54 per share, at a weighted average sale price of \$3.2644 per share; and (3) On May 4,
13 2020, Pourhassan sold 1,201,652 shares of CytoDyn common stock at prices ranging from \$2.53
14 to \$3.00 per share, at a weighted average sale price of \$2.7904 per share.

15 20. The same Form 4 disclosed that Pourhassan exercised the options and sold the
16 2,000,000 shares awarded to him in the December 2019 Grant.

17 **III. Pourhassan violated Section 16(b) of the Exchange Act.**

18 21. Section 16(b) of the Exchange Act provides that:

19 **Profits from purchase and sale of security within six months.** For the purpose
20 of preventing the unfair use of information which may have been obtained by
21 such beneficial owner, director, or officer by reason of his relationship to the
22 issuer, any profit realized by him from any purchase and sale, or any sale and
23 purchase, of any equity security of such issuer (other than an exempted security) .
24 . . . within any period of less than six months . . . shall inure to and be
25 recoverable by the issuer.
26

22 22. The December 2019 Grant is not an exempt purchase and Pourhassan’s sale of 4.8
24 million shares in April and May 2020 are not exempt sales. Accordingly, Pourhassan’s deemed
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1 purchase and sale of CytoDyn's securities within six months is a violation of Section 16(b) of the
 2 Exchange Act, and Pourhassan's statutory profits from the Sales are recoverable by CytoDyn.

3 **IV. Pourhassan cannot claim any exemption.**

4 23. SEC Rule 16b-3 provides an exemption from Section 16(b) of the Exchange Act
 5 in connection with transactions between an issuer and its directors and officers. The December
 6 2019 Grant was a transaction between the issuer (CytoDyn) and Pourhassan (an officer/director)
 7 in which Pourhassan received 2,000,000 stock options.

8 24. Rule 16b-3 states that "a transaction between the issuer . . . and an officer or
 9 director of the issuer that involves issuer equity securities shall be exempt from [S]ection 16(b)
 10 of the [Exchange] Act if the transaction satisfies the applicable conditions set forth in this
 11 section."

12 25. Specifically, under Rule 16b-3(d)(1), a "[a]ny transaction, other than a
 13 Discretionary Transaction, involving an acquisition from an issuer (including without limitation
 14 a grant or award), whether or not intended for a compensatory or particular purpose, shall be
 15 exempt [from Section 16(b) of the Exchange Act] if . . . [t]he transaction is approved by the
 16 board of directors of the issuer, or a committee of the board of directors that is composed solely
 17 of two or more Non-Employee Directors."

18 26. The other Section 16(b) exemptions under Rule 16b-3(d) are: (1) advance
 19 approval of the transaction by a majority of the Company's security holders (the "Majority
 20 Security Holder Exemption"); and (2) the utilization of a six-month holding period by the officer
 21 or director who acquired the securities from the issuer (the "Six Month Holding Period
 22 Exemption"). *See* Section 16b-3(d)(2) and (d)(3) of the Exchange Act; *see also* PETER J. ROMEO
 23 & ALAN L. DYE, SECTION 16 TREATISE AND REPORTING GUIDE, §14.02, at 1386-87 (4th ed. 2012)
 24 [hereinafter "SECTION 16 TREATISE"].

25 27. Pourhassan's December 2019 Grant does not qualify for the exemption under
 26 Rule 16b-3(d)(1) because the December 2019 Grant was not: (1) approved by each member of

1 CytoDyn's Board in December 2019 (the "Board Approval Exemption"); or (2) approved by a
 2 committee of CytoDyn's Board that was composed solely of two or more non-employee
 3 directors (the "Non-Employee Director Committee Exemption").

4 28. The Board Approval Exemption only applies to a transaction if all procedural
 5 requirements for board approval of the transaction are met. *See* SECTION 16 TREATISE, §
 6 14.06[3], at 1432. These procedural requirements include approval by the Company's "full
 7 board" of directors, i.e., *each board member*. *See* SECTION 16 TREATISE, §14.06[4][a], at 1433
 8 (citing *American Society of Corporate Secretaries*, SEC No-Action Letter, Q.1(b) (December 11,
 9 1996) (absent approval by non-employee directors with full authority under Rule 16b-3(d)(1)
 10 "only approval by the full board of directors would be sufficient under the rule"); SECTION 16
 11 TREATISE, §14.06[3], at 1432 (citing *American Society of Corporate Secretaries*, SEC No-Action
 12 Letter, Q.1(b) (December 11, 1996) (when engaging in the advance approval process under Rule
 13 16b-3(d)(1), the "*full board* may consider non-binding recommendations by a committee of
 14 directors") (emphasis added). Indeed, the SEC issued guidance under the Section 16b-3(d)
 15 exemption clarifying that board approval must involve the "full board." *See Exchange Act*
 16 *Section 16 Related Rules and Forms*, U.S. SEC. AND EXCH. COMM'N (2010),
 17 <https://www.sec.gov/divisions/corpfin/guidance/sec16interp.htm> (noting that approval by a "full
 18 board" is one of the conditions under the Rule 16b-3(d) exemption).

19 29. The SEC consistently referred to the Board Approval Exemption as requiring
 20 approval by the "full board." In 1996, the SEC broadened the Rule 16b-3 exemption by
 21 eliminating a requirement that the grant needed to be pursuant to an employee benefit plan. *See*
 22 *Ownership Reports and Trading by Officers, Directors and Principal Security Holders*, 70 Fed.
 23 Reg. 46,080, 46,081-82 (Aug. 9 2005). In proposing this change, the SEC noted that "approval
 24 by the *full board* or a committee comprised solely of two or more non-employee directors would
 25 be retained as an alternative basis for exempting grants and awards." *See Ownership Reports and*
 26 *Trading by Officers, Directors and Principal Security Holders*, 60 Fed. Reg. 53,832, 53,834

1 (Oct. 17, 1995) (emphasis added). In its final rule in 1996, the SEC noted that “when [Rule 16b-
 2 3] requires ‘Non-Employee Director,’ *full board*, or shareholder approval, the [Securities and
 3 Exchange] Commission intends that approval relate to specific transactions rather than the plan
 4 in its entirety.” *See Ownership Reports and Trading by Officers, Directors and Principal*
 5 *Security Holders*, 61 Fed. Reg. 30,376, 30,381 (June 14, 1996) (emphasis added).

6 30. In addition to the SEC’s pronouncements, federal courts, including the United
 7 States Court of Appeals for the Ninth Circuit, also confirmed that the Board Approval
 8 Exemption requires approval of the Company’s “full board.” *See Dreiling v. Am. Express Co.*,
 9 458 F.3d 942, 954 (9th Cir. 2006) (citing *Ownership Reports and Trading by Officers,*
 10 *Directors and Principal Security Holders*, 61 Fed. Reg. 30, 381 (June 14, 1996)) (noting that
 11 Rule 16b-3(d) requires “full board” approval); *Segen v. CDR-Cookie Acquisitions, L.L.C.*, 2006
 12 U.S. Dist. LEXIS 3053, at *5 (S.D.N.Y. Jan. 4, 2006) (noting that, among other reasons, because
 13 “Covansys’s *full board of directors* . . . approved the transaction and recommended it to the
 14 company’s shareholders,” the transaction was exempt under Rule 16b-3) (emphasis added); *Atl.*
 15 *Tele-Network v. Prosser*, 151 F. Supp. 2d 633, 638 (D.V.I. 2000) (citing *Skadden, Arps, Slate,*
 16 *Meagher & Flom LLP, SEC No-Action Letter*, [1999 Transfer Binder] Fed. Sec. L. Rep. (CCH) P
 17 77,515, at 78, 565-66 (Jan. 12, 1999)) (“If *full board approval* . . . is to be relied upon to exempt
 18 the transactions, this approval must specify . . . that the approval is granted for purposes of
 19 exempting the transaction under Rule 16b-3”) (emphasis added).

20 31. Here, Pourhassan’s December 2019 Grant was not approved by CytoDyn’s full
 21 December 2019 Board. Instead, the December 2019 Grant was approved by only three of the five
 22 members of the December 2019 Board: Kelly, Welch, and Klump.

23 32. In addition to Pourhassan, who did not cast a vote, Naydenov was not present at
 24 the meeting and did not approve Pourhassan’s December 2019 Grant.

25 33. Thus, the Board Approval Exemption does not apply to the December 2019
 26 Grant.

1 34. At the same time, the December 2019 Grant also fails to qualify for the Non-
2 Employee Director Committee Exemption. Under Rule 16b-3(b)(3), a Non-Employee Director is
3 one who “[d]oes not receive any compensation, either directly or indirectly, from the issuer
4 for services rendered as a consultant or in any capacity other than as a director.”

5 35. As explained above, Pourhassan’s December 2019 Grant was approved by only
6 three of five members of the December 2019 Board. Critically, this incomplete version of
7 CytoDyn’s full Board included *only one* non-employee director. Of the three directors who
8 approved the December 2019 Grant – Kelly, Welch, and Klump – only Klump was a non-
9 employee director within the meaning of Section 16(b).

10 36. During the December 19, 2019 Board Meeting, Pourhassan was not a non-
11 employee director because he was the Company’s CEO. Kelly and Welch became paid
12 consultants for the Company in July 2019, and neither director qualified as a “non-employee
13 director” for purposes of SEC Rule 16b-3(b)(3). As conceded by the Company in its public
14 filings, Kelly and Welch’s consulting agreements also rendered them not “independent” under
15 NASDAQ Rules.

16 37. Naydenov, the only other person who qualified as a non-employee director for
17 purposes of Rule 16b-3(b)(3) at the time, was not present at the meeting in which Pourhassan
18 received his December 2019 Grant and did not approve the transaction.

19 38. Accordingly, the December 2019 Grant does not qualify for the Non-Employee
20 Director Committee Exemption under Rule 16b-3(d)(1).

21 39. The transaction cannot be deemed exempt under Rule 16b-3 because
22 Pourhassan’s December 2019 Grant was approved by less than the full Board and by *only one*
23 non-employee director. In creating the Rule 16b-3 exemption, the SEC focused on ensuring that
24 “appropriate company gate-keeping procedures are in place to monitor any grants or awards and
25 to ensure acknowledgement and accountability on the part of the company when it makes such
26

1 grants and awards.” *See Ownership Reports and Trading by Officers, Directors and Principal*
 2 *Security Holders*, 60 Fed. Reg. 53,835 (Oct. 17 1995).

3 40. Rule 16b-3 cannot logically be construed to mean that the exemption applies
 4 where, as here, the transaction is approved by a subset of the board of directors, i.e., a de facto
 5 committee, *and* this subset includes *only one* non-employee director. An ability to claim the
 6 “full” Board Approval Exemption in this situation makes no sense. A contrary reading would
 7 apply the Board Approval Exemption to committees of directors comprised of a majority of the
 8 board but just one non-employee director. This would completely negate the point of the Non-
 9 Employee Director Committee Exemption and contradict Rule 16b-3’s purpose and history.

10 41. The December 2019 Grant did not satisfy the Six-Month Holding Period
 11 Exemption because Pourhassan exercised the December 2019 Grant and sold the 2,000,000
 12 shares underlying that grant between April 30, 2020 and May 4, 2020, less than six months from
 13 the date of the December 2019 Grant.

14 42. The Sales are not exempt, as these were open market sales. *See* SECTION 16
 15 TREATISE, § 7.06, at 645.

16 43. No other exemptions apply to the December 2019 Grant or the Sales.

17 44. Thus, Pourhassan violated Section 16(b) of the Exchange Act by purchasing and
 18 selling CytoDyn common stock within six months. Accordingly, Pourhassan is required to
 19 disgorge the profits he unlawfully obtained.

20 **ALLEGATIONS AS TO DEMAND**

21 45. On May 21, 2020, Plaintiffs made a demand on CytoDyn to compel Pourhassan to
 22 disgorge the profits he unlawfully obtained through his violation of Section 16(b) of the
 23 Exchange Act (the “May 2020 Demand”).

24 46. On May 25, 2020, CytoDyn’s Vice President, General Counsel, and Corporate
 25 Secretary, Arian Colachis (“Colachis”), responded to Plaintiffs’ May 2020 Demand, stating that
 26

1 the December 2019 Grant was an exempt purchase from Section 16(b) of the Exchange Act
2 under Rule 16b-3.

3 47. On June 2, 2020, Plaintiffs responded to Colachis, noting that the December 2019
4 Grant actually was not exempt under Rule 16b-3, as neither CytoDyn's full Board at the time nor
5 a committee of two or more independent directors approved the December 2019 Grant. Plaintiff
6 also noted that neither the stockholder approval nor the six-month holding period exemptions
7 applied.

8 48. On June 18, 2020, Colachis responded to Plaintiffs and asserted, once again, that
9 Pourhassan's December 2019 Grant was an exempt purchase, and that accordingly it was not
10 matchable for purposes of Section 16(b) of the Exchange Act. (The correspondence described in
11 paragraphs 45-48 is attached hereto as Exhibit 1.)

12 49. Under Section 16(b), "suit to recover such [short-swing] profit may be instituted
13 at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any
14 security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to
15 bring such suit within sixty days of request or shall fail diligently to prosecute the same
16 thereafter" Accordingly, as CytoDyn failed to disgorge Pourhassan's profits from the
17 December 2019 Grant and the Sales, Plaintiffs commenced this action.

18 50. Recovery of profits under Section 16(b) is computed by using the "lowest-in,
19 highest-out" method in which the highest sale price is matched with the lowest purchase price
20 within six months. On December 19, 2019, CytoDyn's stock price was \$0.63 per share, which is
21 the deemed purchase price for the 2,000,000 stock options Pourhassan acquired on that date. The
22 highest price per share Pourhassan obtained in the Sales was \$3.74 per share on April 30, 2020.
23 Accordingly, CytoDyn's recoverable profit for Pourhassan's violation of Section 16(b) is
24 \$6,220,000.

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26 //

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CAUSE OF ACTION
Violation of Section 16(b) of the Securities
Exchange Act of 1934, 15 U.S.C. § 78p(b)

51. Plaintiffs re-allege each allegation contained above as if set forth herein.

52. On December 19, 2019, Pourhassan was granted 2,000,000 stock options at a Board meeting where only four out of five members of the Company's Board at the time were present and only one member was a non-employee director within the meaning of Section 16(b). Pourhassan did not hold the shares underlying the award for six months. Accordingly, the December 2019 Grant is not exempt under SEC Rule 16b-3.

53. On April 30, 2020, May 1, 2020, and May 4, 2020, less than six months after being awarded the December 2019 Grant, Pourhassan sold 4.8 million shares of CytoDyn common stock in a non-exempt open market transaction, thus violating Section 16(b) of the Exchange Act.

54. As a result, Pourhassan improperly garnered short-swing profits in violation of Section 16(b).

55. Pourhassan is subject to strict liability for his violation of Section 16, and his profits must be disgorged and returned to CytoDyn.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs request entry of an order as follows:

A. Requiring Defendant Pourhassan to account for and pay over to CytoDyn the short-swing profits recoverable from him under Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78p(b), together with appropriate pre-judgment and post-judgment interest and costs of this suit;

B. Awarding Plaintiffs the costs and disbursements of this action, including reasonable allowance of fees and costs for Plaintiffs' attorneys, experts, and accountants; and

1 C. Granting to Plaintiff such other further relief as the Court may deem just and
2 proper.

3 DATED this 10th day of September, 2020.

4 s/ Rylan Weythman

5 s/ Kelly A. Mennemeier

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